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ABSTRACT

In fall 1978, Paul Gann, who worked with Howard Jarvis to pass California's Proposition 13 in June 1978, sought to qualify an intitiative placing a constitutional limit on state and local government expenditures. This initiative qualified and was approved by voters in November 1979 as Proposition 4. Gann's solicitation set the limitation's base year at 1978-79. Annual increases in the appropriation limit would be no greater than changes in the U.S. Consumer Price Index plus population. The initiative petition's signers expected future per capita government expenditures to be equal in real dollars to the 1978-79 level, since the annual adjustment would reflect the change in the cost-of-living. Inadequate attention was given the material that Gann circulated. The initiative restricted an annual increase in the Gann appropriation limit that has failed to conform to the intent of Proposition 13. Because the increase in per capita personal income was lower than the percentage increase in the consumer price index for three years (1980-81, 1981-82, and 1983-84), the annual growth in the appropriation limit was also lower than the promised cost-of-living and population increase. The resultant revenue deficiency and related problems are discussed at length in this paper. Unless voters approve a constitutional amendment to change the Gann formula, the situation of state and local government agencies (including school districts) will worsen in the future--especially if the economy experiences another period of stagflation. Governor Deukmajian's establishment of $1 billion reserve in the 1987-88 budget only compounds the problem, since surplus revenues inside the appropriations limit must be returned to taxpayers. This system shortchanges schools and community colleges, as may be seen from supportive statistics. Included are two tables and the "spirit of 13" campaign flyer. (MLH)

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GANN LIMIT & PROPOSITION 13:
Negative Effects on Local Government Agencies, Including Schools & Community College Districts

Albert S. Rodda, Ph D
Los Rios Community College District
Board of Trustees
October, 1987

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You are informed, I know, about the problems relating to the Gann Limit. This paper includes an analysis of problems which relate to Proposition #13. The relation between the two is discussed and might be of interest to you.

PART I -- GANN LIMIT DEFICIENCY

In the Fall of 1978, Paul Gann, who worked with Howard Jarvis to gain voter approval of Proposition #13 in June of 1978, sent out a letter of solicitation for signatures to qualify a second constitutional amendment initiative for the ballot in 1979. The objective of the initiative was to place a constitutional limit on government expenditures, state and local, in California. It qualified and was approved in November 1979 and is identified as Proposition #4.[1]

In his solicitation, he stated that 1978-79 would be the base year for the limitation and that annual increases in the Appropriation Limit, as it was defined, would be no greater than the "changes in the Consumer Price Index (U.S.) plus population," and this language was interpreted by the voters to be the essential provision of the initiative when they approved it on November 6, 1979. It was expected, therefore, by those who signed the initiative petition that the future per capita government expenditures would be equal in real dollars to the level which was provided in fiscal year 1978-79, since the annual adjustments would reflect the change in the cost-of-living.

Inadequate attention was given to all of the material that Gann circulated, including a draft of the proposed initiative which contained the following language: "...cost-of-living shall be...the Consumer Price Index for the U.S. as reported by the U.S. Department of Labor or successor agency of the U.S. government; provided, however, that for purposes of Section 1, the changes in

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[1]A copy of letter of solicitation is on the last page of this paper.

the cost-of-living from the preceding year shall in no event exceed the change in California per capita personal income from the preceding year."

Since that language was identical to the initiative approved by the voters, the initiative placed a restriction on the annual increase in the Gann Appropriation Limit which has failed to conform to the intent as stated in the "Spirit of 13, Inc." signature solicitation petition. The reason for that deficiency is that for three years, 1980-81, 1981-82, and 1983-84, the increase in per capita Personal Income was lower than the percentage increase in the Consumer Price Index and the annual growth in the Appropriation Limit, therefore, was lower than the increase in the cost-of-living and the increase in population promised in the solicitation.

In 1986-87, six years after the initiative became effective, the Gann Limit factored out at $23.8 billion and reflected a 90% increase over the 1978-79 base year. In the same year, if the formula used to determine annual increases had been, as stated by Gann in his letter of solicitation, the CPI and Population, the Appropriation Limit would have been $25.3 billion or a 102% increase. The net difference between the two amounts to $1.5 billion, which means that had the changes in the CPI been utilized in the calculation the dollar amount of the 1986-87 Gann Appropriation Limit would have been 6% more than the Gann Limit which became effective in that year.

If the Gann formula had been adjusted for changes in Personal Income and population growth alone, the state's Gann Limit would have equalled $28.7 billion for 1986-87, an increase equal to 130% and the net dollar difference

would have been $4.9 billion. Such a level, if established for the Gann Limit, would reflect, not only inflation and the population increase, but the improvement in the state's economy because of economic growth, since the Index of Personal Income is a measurement of changes in the personal income experienced by the citizens as a consequence of changes in the state's economic productivity.

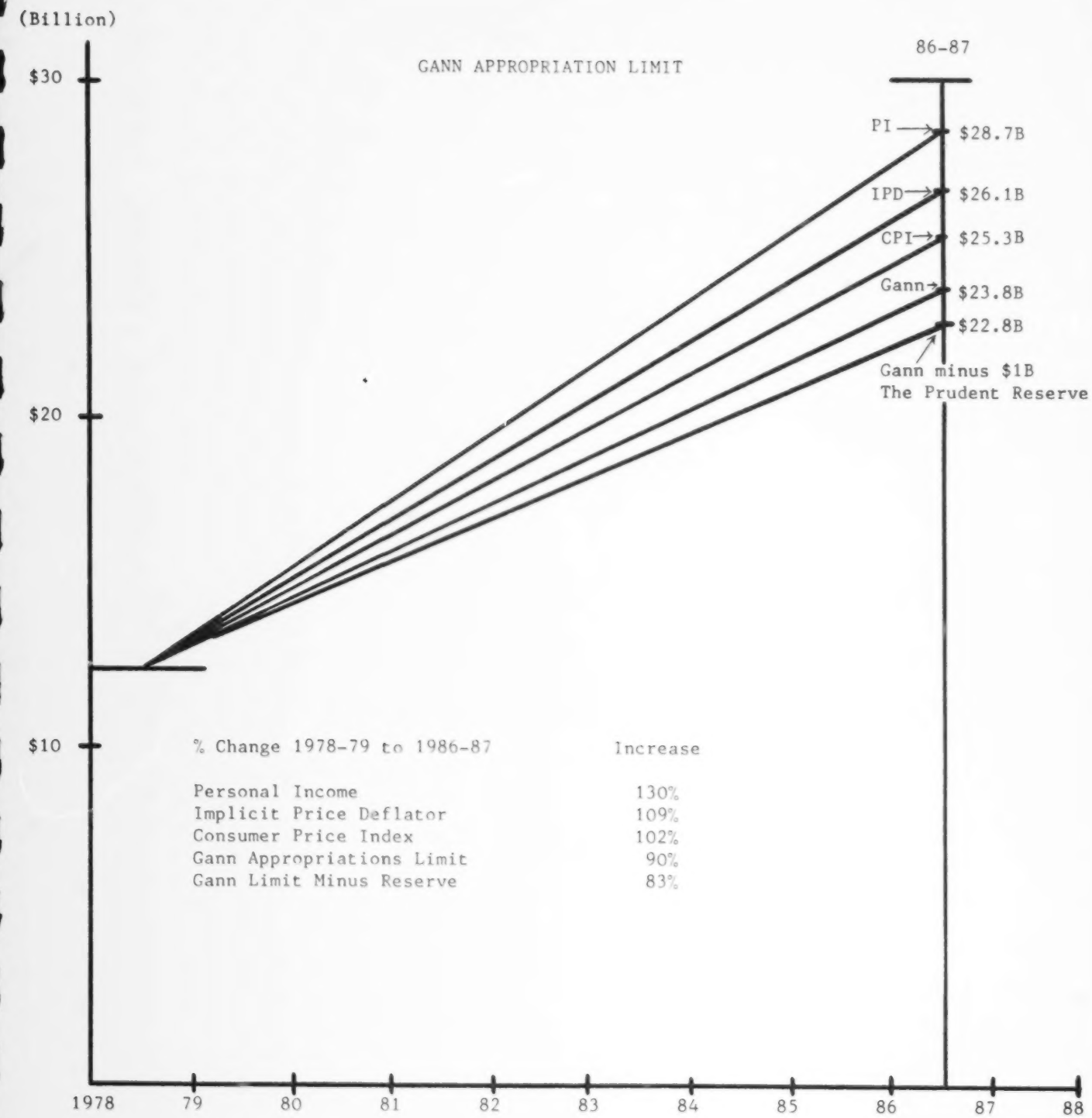
Another meaningful index is the Implicit Price Deflator for State and Local Government Purchases, which is a measurement of annual changes in the cost of purchases made by the state and local segments of government. If the Gann Limit formula had been adjusted annually to reflect the Implicit Price Deflator (IPD), the limit in 1986-87 would have amounted to $26.1 billion, or 3% greater than the Gann Limit, or a difference in the amount of $800 million.
When calculated on a per capita basis, the Gann Appropriation Limit factored out at $882 in 1986-87 and when calculated on the basis of increases in the CPI and population, it amounted to $937. An even more dramatic difference prevails, however, when a comparison is made between the Gann formula and annual increases based exclusively upon annual percentage changes in Personal Income and the population. On the basis of such a calculation, the per capita Gann Limit would have been to $1,060. If the Implicit Price Deflator were used, the per capita Gann Limit for 1986-87 would have been approximately $974.

It must be recognized that fiscal year, 1986-87, was a critical year, since it was the first year that the state was required to comply with the Gann mandated tax rebate, a rebate in the amount of approximately $1.1 billion. It is interesting, however, that while the state, because of a favorable revenue

situation, is spending at the Gann Limit level, many agencies of local government and local school districts, including community college districts, will have to operate under 1987-88 budgets which will be below the appropriations authorized by the Gann Limit. The Los Rios Community College District, for example, is estimating that the district will be compelled to operate under a 1987-88 budget which will authorize expenditures approximately 7.2% less than allowed under the district's Gann Limit. In dollars, the difference amounts to approximately $5.3 millions. This problem, one of a revenue deficiency, is proving quite serious, and I will discuss it in detail in Part III of this paper.

Absent voter approval of a constitutional amendment which changes the Gann formula, this situation with respect to the state and local agencies of government will become even more severe in the future, and it will become even worse if the economy experiences another period of stagflation, which is the term used to describe an economic condition in which there is an economic recession during a period of price inflation. During such difficult economic circumstances the Gann Limit will not increase at a rate equal to the depreciation of the dollar, or inflation as measured by the Consumer Price Index.

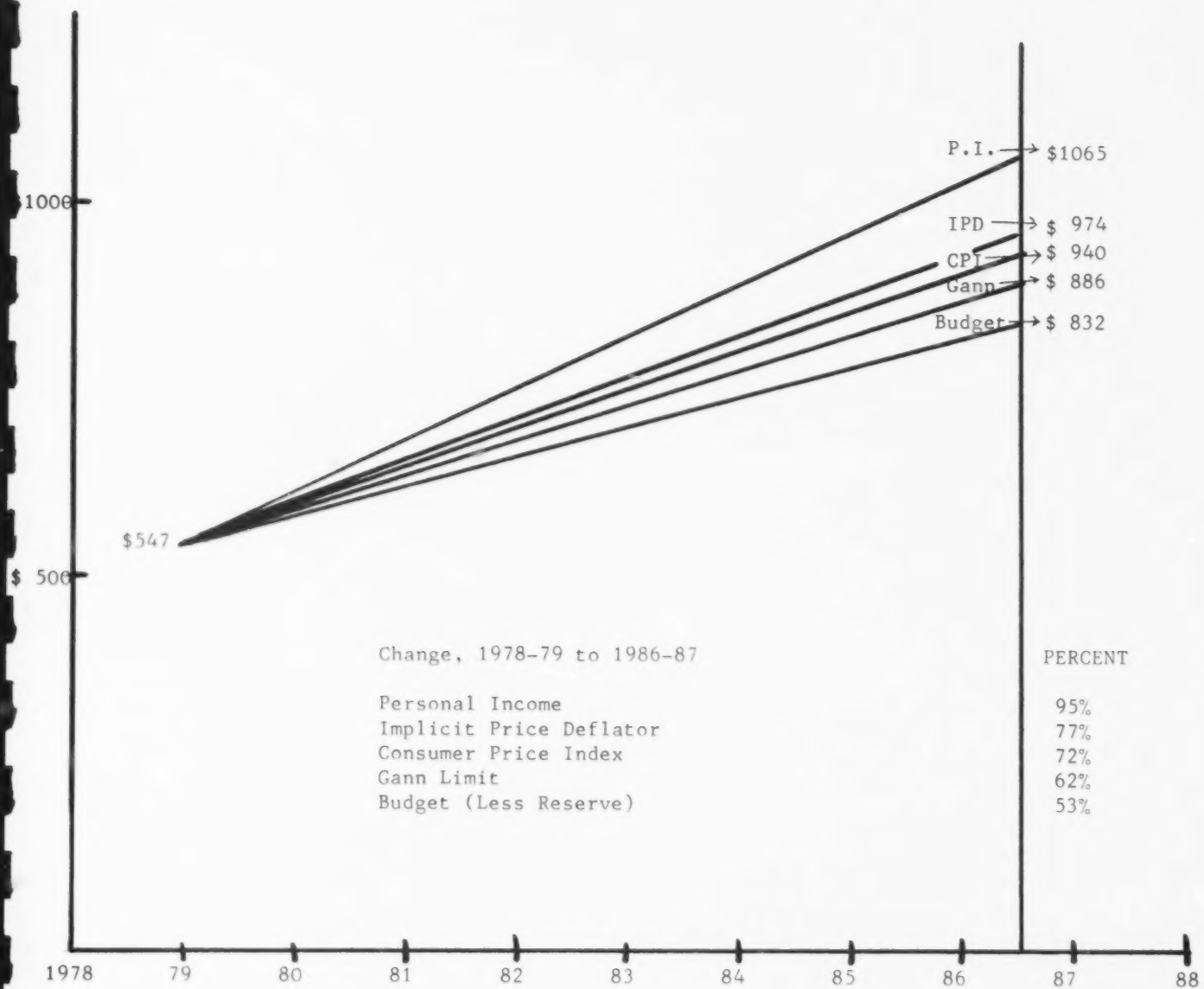
In considering a change in the formula, the minimum correction should be one that provides a formula which will, in the language of the Gann solicitation, adjust each year's Appropriation Limit so that it reflects "...changes in the Consumer Price Index (U.S.) plus population." The enclosed charts reflect the



% Change 1978-79 to 1986-87	Increase
Personal Income	130%
Implicit Price Deflator	109%
Consumer Price Index	102%
Gann Appropriations Limit	90%
Gann Limit Minus Reserve	83%

[1] As introduced, the budget for 1986-87 provided for a reserve of about $950 million. At the end of the fiscal year, the reserve was approximately $550 million. The budget for 1987-88 establishes a Prudent Reserve of $1 billion.

PER CAPITA APPROPRIATION LIMIT



Change, 1978-79 to 1986-87	PERCENT
Personal Income	95%
Implicit Price Deflator	77%
Consumer Price Index	72%
Gann Limit	62%
Budget (Less Reserve)	53%

difference between the Gann Limit as calculated on the basis of different measurements of changes in the economy--inflation and economic growth.[2]

Part II--Impact of a Prudent Reserve

An interesting aspect of the impact of the initiative is that it allows agencies of government to maintain prudent reserves against unforeseen economic circumstances and contingencies but it does not allow the reserves to be maintained outside of or above the Appropriation Limit. The result is, therefore, to accentuate the adverse effect of the Gann Limit upon real dollar state government expenditures. The reason is that when the base year, 1978-79, was determined, the state was involved in the Proposition #13 bailout of local governments and the schools in an amount equal to about $4.4 billion, which provided a partial offset of the $7 billion lost because of the effect of the initiative upon local property tax revenues. The state did not include a Prudent Reserve in its budget appropriations, and, therefore, the surplus it carried forward into the next year was not a part of the base year Gann Appropriation Limit calculation. The calculations for the base year resulted in a Gann Limit equal to $12.5 billion which was equal to the state's total appropriations for that year. Today, when the state budget includes a surplus or Prudent Reserve, it is considered a part of the state budget and is included in the state appropriations which are subject to the Limit. The result is that

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[2]The Gann Limit estimates do not conform to those made by the Department of Finance because of the fact that the Department added dollar amounts to its Gann Limit calculations which have been questioned by the Office of Legislative Analyst and which I excluded. Because of the dollar augmentations, the Department of Finance has established state Gann Limits at a higher level. The disagreement over the appropriateness of the dollar augmentation has not been resolved as of yet and may ultimately be decided by the judiciary.

the state Prudent Reserve reduces the appropriations which may be authorized to fund government services under the Limit by an amount of dollars equal to the dollars set aside as a reserve.

Because of Governor Deukmejian's experience with the 1982-83 state budget revenue shortfall in his first year as Governor, he has been adamant in his determination to set aside a minimum of approximately $1 billion in the form of a reserve against unanticipated contingencies. Since this $1 billion reserve has been provided in the 1987-88 budget and is calculated under the Gann Limit as a state expenditure, it compounds the problem the state is experiencing in adjusting to an expenditure control which, as I have calculated, is approximately $1.5 billion below what it would be if measured against a Limit which reflected changes in the CPI and population.

When these two negatives are added together, it is clear that the Gann Appropriation Limit is approximately $2.5 billion less than the amount necessary to assure the state that the per capita real expenditure in 1978-79 is maintained in 1987-88, nine years later. It amounts to about a 10% erosion in 1978-79 dollars.

It is only reasonable to argue, therefore, that the Gann Appropriation Limit should be changed in order to permit the maintenance of a responsible Prudent Reserve Against Economic Uncertainties which is outside and not within the Appropriation Limit. In fact, such a change is now being supported by Gann and his associates.

Part III -- Gann Limit and Revenues

An interesting aspect of the current fiscal situation is the relation of government revenues to the Gann Limit, one which varies significantly among agencies of local government, cities and counties, and school districts, K-14. Some are close to their limits and others are significantly below their limits.

And while this fiscal confusion prevails at the local level and can be expected to continue into the future, the state, because the elasticity of its revenues[3] exceeds the elasticity of the state Gann Limit, can be expected to experience revenue surpluses in the future which may not be utilized to finance state government programs. Many school districts, cities and counties, however, will be mired in an impossible situation--inadequate Gann Appropriation Limits and revenues below those necessary to finance educational and government services authorized by the Gann Limit levels.

The problem confronting local governments, of course, is directly related to the fact that their revenues, especially property tax revenues, are less elastic than their Gann Limits, which despite the acknowledged deficiency in the Gann formula in adjusting for inflation and population changes will increase at a more rapid rate than revenues, unless, of course, some changes are made in the state's fiscal and revenue structure, state and local.

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[3]Elasticity is the percentage increase in revenues compared to the percentage increase in Personal Income. If the increase is the same, elasticity is unity, or 1. If it is greater by 10%, the elasticity is 1.1; if it is lower by 10%, it is .9, or inelastic.

Revenues at the state level are currently exceeding the Gann Appropriation Limit, a change from the pattern which prevailed during the first seven years of the Gann Limit, 1979-80 through 1986-87. In the first year of the implementation of Gann Limit, 1980-81, the state was meeting its budget expenditures through the use of carry over surpluses to supplement tax revenues which were not producing a level of state income equal to the Gann Limit--a condition which continued during the early eighties because of the adverse effect upon tax revenues of the recession experienced by the economy. As late as last year, the state's revenue deficiency was expected to continue through 1986-87 and possibly into 1987-88. To the surprise of the Deukmejian administration experts in state finance, who were making such predictions, the economy improved and generated a substantial increase in state revenues over the amount projected for 1986-87 and 1987-88. Unfortunately, because of the inability of the Legislature and the Governor to agree on the way in which the revenue increase should be utilized in the 1987-88 budget, appropriate legislation was not enacted, and the state, therefore, was confronted with a situation in which revenues in fiscal year 1986-87 exceeded the estimated Gann Appropriation Limit in the amount of approximately $1.1 billion dollars, including a reserve in the amount of $571 million. It is estimated that the state budget for 1987-88 will be within the Gann Limit and will include a Prudent Reserve of about $1.0 billion.

Had a compromise on the issue been achieved, a substantial portion of the state Gann Limit excess could have been allocated to local agencies and local school districts, K-14, in the form of state subventions which would be included in the local and not the state Gann Appropriation Limit.

As a consequence of the partisan political impasse, significant state tax revenues are being returned to the taxpayers, beginning in November of this year, while many agencies of local government and school districts, K-14, will have to cope with serious, if not almost impossible, budgetary problems[4].

The history of the current fiscal situation for state and local governments is interesting. Unfortunately, the problem is not only serious, but it is quite complicated, and any substantive reform will prove controversial.

During the seventies a powerful tax revolt movement developed in the state and, as a consequence of the desperate need for the state to respond, the Legislature placed before the voters a property tax relief-reform statute which would have reduced property taxes thirty percent across the board, provided greater relief for senior citizens who were home owners or renters, and required the state to assume the local costs of SSI-SSP, Medi-Cal and AFDC. The proposal was rejected by the voters in favor of Proposition #13, which imposed upon local governments and the schools, K-14, a $7 billion reduction in property tax revenues. Since the result would have been devastating for fiscal year 1978-79, the state committed itself to a one-time bailout of local government and school districts. In the following year, the bailout was made ongoing through the enactment of AB 8, Greene. As a part of that legislation approximately $800 million in local property tax revenues were shifted from the schools, K-14, to other local agencies of government.

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[4]Legislation was enacted during the closing hour of the session which authorized a modest dollar allocation to urban school districts. The school allocation was $86.6 million. Prior to that action, the Governor vetoed a school apportionment bill which would have granted an additional $700 million to public education, K-14.

One of the consequences of that action was to make the schools, K-14, more dependent upon the state for funding and to increase local governmental dependence upon the local property tax revenues. In those areas where there has been growth and development the fiscal situation has been favorable to the cities and counties; however, in those areas where there has been an absence of such development, the fiscal consequences of Propositions #13 and AB 8 have been unfavorable and current statistical data indicate that local agencies of government are suffering financially, and many now have annual revenues which are significantly below their Gann Appropriation Limits.

This, of course, is a result of the fact that under Proposition #13 when new construction is taxed, the property is assessed at the current market value, which is true also of property which changes ownership, but all other property is assessed annually to reflect only a 2% increases, the base year being the 1975-76 assessed value. Local revenues, therefore, in slow growth areas are increasing only at a modest rate and one which is not equal to the rate of increase in the Gann Limit.

Absent a determination on the part of the state to recognize this problem, local public services in areas of the state where there is a slow rate of growth will suffer seriously.

Voters may, under the provisions of Proposition #4, increase the local Gann Limit, but a voter approved expenditure limit increase may continue only for four years unless approved a second time by the voters. Any such action taken by the voters, therefore, will amount to a band-aid approach to a serious

fiscal issue confronting those segments of government which are not experiencing favorable economic growth.

A change in the Gann Limit formula, though warranted, will not benefit local governments in slow growth areas, since the current problem is not a deficient expenditure authorization. It is a deficient revenue source. Unless the revenue situation improves, a greater annual increase in the Gann Appropriation Limit, resulting from a change in the formula, will merely widen the gap between revenues and the Gann appropriation authorization. Of course, those agencies of government in rapid growth areas will benefit, since they will be able to spend revenues they receive but may not appropriate under the current formula.

The fact of reality is that whereas the state will exceed the Gann Limit this year, 1986-87, and will return $1.1 billion to the taxpayers, most local agencies of government and school districts, K-14, are receiving cumulatively revenues, on the whole, below the Gann Limit. The difference varies, of course. Some counties and cities are spending at a level close to their Gann Limits and suffer primarily from the inadequacy of the Gann Limit formula to reflect adequately changes in the real value of the dollar. They would benefit from a change in the Gann Limit formula which made it reflect more realistically annual changes in inflation.

The state of California is fairly immune from this adverse fiscal circumstance in view of the fact that its revenue situation has not suffered a serious deterioration since 1978, the year Proposition #13 was approved by the voters.

The reason is that the state is not dependent upon the property tax for revenues. One adverse effect of Proposition #13 upon the state, however, was the fiscal burden it had to assume in order to bailout the schools and local agencies of government. Subsequent to Proposition #13, the voters approved two initiatives which virtually repealed the Inheritance and Gift tax and required the full indexation of the Personal Income tax. That action reduced the annual rate of growth of state revenues, but it has not been significantly adverse, at least as of now. State revenues are now less elastic than they were in the seventies but they still exceed an elasticity of unity, or 1.0, when the condition of the economy is favorable. And, of course, because of the reduction in the level of authorized state expenditures resulting from Proposition #4, the Gann Limit, state revenues are adequate to finance the state budget. During a period of economic recession, there is a potential for a revenue deficiency and that aspect of state finance warrants the maintenance of a Prudent Reserve, but the situation is not one which may be referred to as "Gloom and Doom," as is the case with respect to a number of counties and some school districts.

During the seventies state revenues increased at a rate greater than that of Personal Income and the elasticity was greater than 1.0, sometimes as high as 1.7. Excluding several exceptional years during the seventies, revenue calculations indicate an elasticity in the magnitude of about 1.35. During the early years of the Reagan administration, however, when the national economy was in recession, the elasticity declined to about .7, or became inelastic. Today, because of improved economic conditions, state revenue elasticity is greater than unity, approximately 1.1, and is estimated to remain at that level

until the economy experiences a decline with the onset of a recession, at which time it can be expected to decline below unity, possibly, depending upon the severity of the cyclical change in the economy, to a level of .7 or .8.

Different revenue sources have different elasticity. The state personal income tax tends to be more elastic than other state taxes. The corporate income tax tends to be elastic but it is a much smaller revenue source. The general sales tax is elastic during periods of economic growth, but sin taxes, those on alcohol and tobacco products, are inelastic, as is the gasoline tax per gallon. The revenues from these taxes are directly related to the number of units sold and that accounts for the lower elasticity.

Since the personal income tax and the tax on corporate income together constitute a large percentage of the revenues received by the state, state revenues tend to be relatively elastic and to provide a reasonable source of total revenues, especially during a period of economic expansion and inflation.

These conditions do not prevail at the local level of government, especially counties and school districts, where tax revenues are related to the local property tax. Prior to Proposition #13, the local property tax tended to be moderately elastic, but because Proposition #13 limits annual increases to 2% of the value of the property, the base year being 1975-76, property tax revenues have lost considerable elasticity, especially in those areas where there is not a high rate of property transfer and modest real estate

development[5]. In such areas local governments do not have a tax or revenue base which increases annually at a rate which reflects inflation and normal increases in the cost of providing government services. It is largely because of this condition that cities, counties, and school districts are experiencing difficulties: one, due to the inadequacy in the Gann Appropriation Limit, and, two, due to the failure of property tax revenues to increase at a rate adequate to finance government services. As indicated above, the problem is worse, in fact very serious, in those geographical areas where there is a low rate of economic development, primarily agricultural and timber producing regions. In areas where enrollment declines are experienced by the schools, K-14, the fiscal situation is made even more negative because revenues from the state are based upon average daily attendance, ADA, as is the Gann Appropriation Limit. Thus, when ADA declines, total school revenues will decline or become stable, depending upon the cost-of-living or COLA adjustments provided through the state funding formula. Of course, the situation varies from area to area; nevertheless, the fiscal situation confronting many school districts and non-growth counties is quite critical. Unfortunately, the local agencies of government and the schools have no power to respond to the situation.

For some counties and special districts, the situation is quite negative because the state does not automatically compensate for property tax revenue declines or inadequacy.

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[5]Between 1984-85 and 1985-86 county appropriation limits increased at a more rapid rate than county revenues in twenty counties. The appropriation limit placed a restriction on eleven counties.

Such a condition can compound over time and, as a result, controlled expenditures which are funded significantly from local revenues may increase at a much lower rate than the rate of increase authorized by the local Gann Appropriation Limit. This can account for the development of a sizeable gap between authorized expenditures and the revenues available to finance them, an unfortunate circumstance which a number of counties have experienced.

Statistical data indicate this situation to prevail in some areas of the state. For example:

Siskiyou in 1984-85 was funded at 66.5% of its Gann Limit and is estimated in 1986-87 to be at a 61.5% level.

Stanislaus in 1984-85 was funded at 63.5% of its Gann Limit and is estimated in 1986-87 to be at a 59.9% level.

Yolo in 1984-85 was funded at 59.9% of its Gann Limit and is estimated in 1986-87 to be at a 57.3% level.

Lassen in 1984-85 was funded at 63.5% of its Gann Limit and is estimated in 1986-87 to be at a 57.8% level.

Similar data relating to counties located in growth areas indicate expenditures equal to a higher percentage of the Gann Limit.

	1984-85	1986-87
San Francisco	95.1%	86.9%
Kern	100.0%	97.2%
Orange	88.0%	92.5%
San Bernardino	87.9%	99.5%
San Mateo	86.2%	92.3%
Solano	92.6%	94.0%
Sonoma	94.4%	98.0%

Shasta County has closed and terminated its countywide library system. The County Supervisors are claiming a $2.6 million shortfall in the county's 1986-87 budget. Butte County is planning to take the same course unless the cities in the county agree to contribute to the support of the library system. Butte County is calculating a revenue shortfall equal to $7.3 million in 1987-88 or 23.6% of its Gann Limit. Tehama is interesting since it has announced that it is bankrupt and that it will be unable to continue providing basic county government services. In 1984-85 the Tehama county limit was $11.7 million and appropriations were $9.6 million, or 82% of the Limit and a shortfall of $2.5 million. In 1985-86 the Tehema County Gann Limit was $12.5 million and appropriations were $10.1 million or 81% of the Limit. The shortfall was $2.37 million. There is no current data available, but it is evident that the fiscal situation is even more negative.

In 1986-87, the aggregate dollar deficiency was serious for those counties which were well below their Limits. The deficiency for El Dorado was $12.6 million and its Limit was $40.1 million; for Siskiyou, it was $2.8 million and

its Limit was $14.1 million; for Trinity, it was $3.3 million and its Limit was $7.8 million; for Tuolumne, it was $9.5 million and its Limit was $21.7 million; for Yolo, it was $19.6 million and its Limit was $46.4 million and for Alpine, it was $2.1 million and its Limit was $3.5 million.

Sacramento County had a Limit of $201 million and a revenue deficiency of $31.7 million, or 15.8% below its Limit.

For the year, the total of the fifty-eight county appropriation limits equaled $6.37 billion; total revenues available to finance expenditures, however, equalled $5.59 billion. The revenue shortage for all counties amounted to $783 million, or a deficiency of 12%.

Similar fiscal problems confronted school districts which had revenues less than or below the Gann Limit, including community college districts.[6]

The percentage of revenues to district Gann Appropriation Limits for 1985-86 for community college districts indicated the following:

North Orange was 58%; Victor Valley was 57.5%; West Kern was 55.1%; Fremont-Newark was 54.7%; Gavalin was 51.8%; Yuba was 50.8%; San Jose was 45.8%; Yuba was 50.8%; Butte was 42.8% and Mt. San Jacinto was 34.1%.

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[6]Sacramento City Unified School District had a 10.1% revenue shortfall; all K-12 districts in the county experienced a 4.6% shortfall and the county office shortfall was 21.9%, or $3 million below the Gann Limit of $15.9 million. ADA declines could be a critical factor with respect to some school districts.

Of course, some districts were experiencing more favorable fiscal situations: Merced was 97.1% of its Limit; Imperial was 95.6%; Palo Verde was 95.5%; Riverside was 92.0%; Allan Hancock was 87.6% and Los Rios was 88.3%.

What these statistics for the community colleges fail to indicate is the disparity that prevailed then and continues to prevail with respect to district revenues per student. For example, the difference, not counting the small districts which have greater expenditures per student, was $870 per student or 35% of the average, which was $2,430 per ADA. West Kern, a wealthy and small district, for example, was spending $6,684 per ADA.

When the entire community college system was taken into consideration the statistical data for 1985-86 indicated that revenues available to all of the 70 districts were equal to approximately 70% of the aggregate Gann Appropriation Limit. The Limit authorized approximately $2.3 billion in expenditures, but the revenues available to the districts equalled approximately $1.6 billion. The shortfall was in the amount of $700 million and it is evident that a similar fiscal situation will confront the community college districts this year, 1987-88, though it will be less serious because of the increase in ADA. The Los Rios shortfall is expected to decline from 12% in 1985-86 to 7.2% in 1987-88, which in dollars amounts to $5.28 million.

The statistical data provide an argument for greater equalization in the financial support provided community college districts, which I previously discussed in another paper, but the data also argue strongly for a change in the funding formula--a change which would provide a more adequate revenue base

in that it would enable the community college districts to fund educational programs equal or close to their Gann Appropriation Limits. Obviously, the issue is complicated, and the important fact of reality is that the districts not only suffer from the effects of an inadequate formula for determining their annual spending limits but from revenue deficiencies which deny them the ability even to fund at a level authorized by an inadequate expenditure limit.

Cities are not being as adversely affected by of a revenue deficiency as are the counties and community colleges since they have a broader local tax base. Furthermore, judicial interpretations of Proposition #13 have allowed cities to increase local tax revenues. Proposition #13 property tax rates, for example, may be increased if the revenues are to finance retirement benefits contracted prior to voter approval of the Jarvis-Gann Limit. The decision was Carman vs. Alvord. In the San Francisco vs. Farrell Decision it was ruled that the two-thirds vote required by Proposition #13 to increase special taxes did not apply if the tax revenues were to finance general fund expenditures, since such taxes would not be classified as "special taxes"as defined under the initiative. As a consequence of this ruling, a number of cities have been able to raise taxes as a means of generating additional revenues. Fewer counties have taken advantage of this court decision because there are more strict statutory limits upon the taxing power of counties than upon city governments.

An interesting fact of California history is that in the early sixties a Governor's Commission on Metropolitan Urban Affairs produced a study relating to local government structure and organization and concluded that there was a need to reduce the number of city incorporations and the creation of special

districts and simultaneously to encourage the creation of regional government units representing the cities and counties in the area for responsible planning. The object of the Commission's recommendations, of course, was to encourage more meaningful planning and development in such areas as transportation, fire and police protection, land conservation, park and recreation development and public education. One outcome was the creation of Local Agency Formation Commissions and because of that action for many years the state has benefitted from a constructive program to provide reasonable and responsible control over the organization and structure of local governments. The effort, however, has not measured up to the goals and objectives of those who were evolved in implementing the concept as an important approach to the issues of conservation and responsible environmental protection.

Unfortunately, because of the negative impact of Proposition #13 on local government revenues, the fiscal benefit of the general sales tax to California cities, and the Supreme Court decision re increases in special taxes, there is an incentive for local communities to seek city incorporation. In the early sixties, for example, Sacramento County had five incorporated areas--North Sacramento, Isleton, Folsom, Sacramento and Galt. Today, after the annexation of North Sacramento by the City of Sacramento, there are only four, and there is the drive to incorporate Elk Grove, Carmichael and Citrus Heights, and in Yolo County, West Sacramento has incorporated. The contemplated incorporation efforts, if successful, will, it appears, deprive Sacramento County of much needed revenues and result in a duplication of government services.

Sacramento County is already suffering from a revenue shortfall because of Proposition #13 and the unrealistic expenditure limit imposed by Proposition #4. Because of these conditions, one can only conclude that community planning will be more difficult and the provision of county services restricted, though the local communities in which incorporation occurs may experience an enhancement of local government services with a potential for tax increases. The future is uncertain. It is clear, however, that community planning and environmental protection have a lower priority today than they had during the sixties and seventies.

In 1986-87 fifty-five cities were within ten percent of their Gann Limits and eighty-one were within 20%. For counties, the statistics were not so favorable. In 1985-86, of the 58 counties, 19 were within 10% of their Gann Limits and 31 were within 20% of their Gann Limits.[7]

It seems apparent that there are at least three changes in California's fiscal situation that are warranted. They are as follows: (1) a formula for calculating annual Gann Limits which more meaningfully conforms to the stated purpose of the designers of the initiative, (2) the exclusion from the Gann

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[7]Rough calculations indicate that in 1981-82 the City of Los Angeles raised approximately 43% of its local revenues from the sales tax and local taxes; whereas, in 1982-83 the County of San Diego generated only 11% of its local revenues from the sales tax and other local taxes. Fees and miscellaneous sources provided 33% of local revenues for the City of Los Angeles in 1981-82 and fees generated 28% of local revenues for San Diego County in 1982-83.

The statistical data for these calculations were derived from a California Tax Foundation Study entitled, "California Local Government Finance: Issues for the 80's." Part I Summary, April 1984. Caution should be exercised in using the data since there is a wide diversity among the cities and counties, as well as between counties and cities.

Appropriation Limit of budget reserves set aside to protect agencies of Government and the schools from the negative impact of a serious decline in revenues, and (3) some adjustment which would enhance revenues received by agencies of government whose revenue base consistently proves inadequate to finance the Gann Appropriation Limit level of services.

Some thought might be given to a program under which state surpluses above a prudent reserve level might be distributed on a formula basis to agencies of local government and school districts suffering from a serious revenue shortfall--revenues less than the appropriation level authorized by the local Gann Limit.

Another concept worthy of consideration is the enhancement in local government revenues. If such a change were to be achieved, of course, a major modification in the Proposition #13 amendment will have to be implemented. It must be recognized, however, that a substantive and realistic change in the basic provisions of Proposition #13 will be unpopular with important elements in the state and that an unrealistic and very idealistic change will result in local revenue losses and, therefore, only compound the negative character of revenue structure upon which local governments are so dependent. Significant and constructive reform will not be easy.

Historically, California has had a fine reputation for the quality of its public services and the character of its infrastructure. The question today, unfortunately, is: Will that tradition be continued? It cannot be preserved under Proposition #13 and #4 as they were approved by the voters.

Signature campaign underway to limit government spending

Spirit of 13 inc.

After months of struggling and failure of the legislature to place a constitutional lid on state and local government spending, Paul Gann, co-author of Proposition 13, has filed to circulate an initiative constitutional amendment. A massive campaign is planned for late October and the first week of November, highlighted by a unique election-day plan to gather signatures from voters as they approach polling places in the state. The initiative would save California taxpayers billions of dollars on an annual basis beginning a very short time after implementation. State spending has increased 13.7 percent annually over the past 10 years while the Consumer Price Index and population have increased at an average of 7.8 percent per year.

Basic provisions of the initiative

1. Limits growth of government: Limits the total annual appropriations of each entity of government — state and local — to changes in the Consumer Price Index (U.S.) plus population.

2. Return of surpluses: Requires government to return surpluses within two years by a revision of tax rates or fee schedules.

3. Vote to exceed limit: May be changed by the electors of such entity, subject to and in conformity with constitutional and statutory voting requirements with an automatic sunset clause for the change.

4. Entities covered: Applies to state, local governments (counties and cities) and school districts.

5. The base year for appropriations: Sets fiscal 1978-79 appropriations as the year upon which the spending limits are based. The base year reflects large expenditure cuts resulting from Proposition 13.

6. Mandates of the state: Requires the state to fund costs of programs it mandates upon local governments occurring after January 1, 1975, from within the state's limit.

7. State subventions to local governments: Includes state subventions in the limit of recipient local agencies but excludes such subventions from the state's limit. This permits the state to meet unforeseen revenue losses due to Proposition 13. Local governments may not use the aid to spend in excess of their own limits.

8. Exempt from the limit: Exempts the following from the limit imposed on each entity of government: 1) expenditures of federal funds, 2) appropriations to comply with mandates of courts and of the federal government, 3) service of existing debt, and future bonded debt approved by the voters, and 4) non-tax-supported government services.

9. Included in limit: This initiative covers all state and local government taxes including, but not limited to, state income tax, state sales tax, property taxes, state and local business taxes, state inheritance taxes, and revenues from regulatory licenses, user charges and fees to the extent that such user charges or fees exceed the actual cost of providing the service, product or regulation.

Paul Gann

10. Other adjustments to limits: Adjusts the spending limitation when the responsibility for funding services is transferred to another entity of government or to a private entity.

11. Contingency fund: Permits each entity of government to establish contingency, emergency or similar fund from the proceeds within that government's appropriation limit. Expenditures from such funds are exempt from the limit.

12. Effective date: The limitation applies to the fiscal year beginning after its adoption.

13. When will it go before the electorate: The measure will not go before the electorate until the June 1980 primary election unless the governor were to call a special statewide election.

Your help is required

Your help is required to qualify this initiative for the ballot. You can play a critical role in the initiative circulation process. If you are available to gather signatures, we urge you to fill out and return the form below together with your generous contribution which will help defray the costs of this campaign.

Volunteers Needed For Initiative Petition Work

Yes, I'll help gather signatures in the upcoming initiative campaign. Please mail me _____ petitions with instructions.

Name _____

Address _____

City _____ Zip _____ Phone ( ) _____

I've enclosed my contribution of $ _____

Send to: SPIRIT OF 13, INC., P.O. BOX 894, SACRAMENTO, CA 95804